Frequently Asked Questions about the Self Insurance Premium

What were the Governor's Risk Management Task Force recommendations?
The task force was comprised of the Attorney General and members representing higher education, public agencies, the private sector and the Legislature.

The Governor and Attorney General proposed legislation to implement several of the task force recommendations. The 2002 Legislature recently enacted all three proposals. Below are the highlights of the task force recommendations and enacted legislation:

- Move the duties and responsibilities of the statewide Office of Risk Management (ORM), currently within the Department of General Administration, to the Office of Financial Management.
- Increase executive involvement in risk management issues. Establish statewide risk management responsibility at a policy level in state government. Provide higher visibility for statewide risk management and risk financing.
- Allow state agencies to express regret to victims without that expression being used against the state in a lawsuit.
- Provide the OFM Director with the discretion to appoint a Loss Prevention Review Team when the death of a person, serious injury to a person, or other substantial loss is alleged or suspected to be caused at least in part by the actions of a state agency. The final Loss Prevention Review Team report and any related documents prepared by or for the team are inadmissible in civil or administrative proceedings, except for impeaching a witness. An agency must respond to the Loss Prevention Review Team's final report within 120 days upon report completion.

Why was the Self Insurance Liability Program created?
In order to fund the expanding liability of the State, the Legislature created a Self-Insurance Liability Program (SILP) for tort liabilities beginning in Fiscal Year 1991. Within the SILP, a Liability Account was established. It paid claims up to $5 million against all State agencies, colleges, boards and commissions and their employees and volunteers (with the exception of the University of Washington and the Washington State Ferry System) from incidents on or after July 1, 1990. A commercial insurance policy (excess policy) with limits of $45 million per year was purchased from agency premiums in 1991 in order to pay any claims exceeding $5 million. Legislation was enacted in 1999 to pay all claims through the SILP regardless of occurrence date and to include payment of the cost of tort defense from the Liability Account. Defense costs were previously paid by individual State agencies. The Liability Account is actuarially based and funded by premiums from State agencies.

What is a tort?
Tort liability is a legally enforceable obligation arising from negligence on behalf of the state. This includes personal injury and property damages to third parties and state employees, excluding worker's compensation. It can also be described as a civil lawsuit to recover damages for the breach of a legal duty. A typical tort is an action for damages resulting from personal injuries caused by negligence.

When does an agency incur a claim liability?
Claims liability is incurred when a claim is filed. Payment of the claim may happen months or years later. The amount to be set aside in the current biennium to cover accrued liability (future tort costs) is a policy decision made by the Legislature. By statute, the amount set aside cannot exceed fifty percent of outstanding liability.

What type of coverage does an agency receive by paying its self insurance premiums?
The Self Insurance Liability Program was designed to pay up to $5 million for each occurrence with the exception of aviation, marine, foreign liability and certain claims involving the acts of students. The Office of Risk Management also purchased an annual commercial insurance policy (Excess Policy). This policy has historically covered claims over $5 million for general liability and $2 million auto liability. An annual policy limit of $45 million was established for each policy year.

The Office of Risk Management was not able to gain as favorable terms on the FY 2002 excess policy due to huge claims payouts during the FY 2001. Consequently, the FY 2002 excess policy covers the following: claim over $15 million for both general liability and auto liability for all agencies except DSHS and DOC. The policy covers claims over $25 million for DOC and DSHS. The FY 2002 policy also excludes coverage for professional liability, errors and omissions, and discrimination claims. The annual policy limit of $45 million is still in place.

How will claim payouts in excess of $15 million be funded for DSHS and DOC?
The Self Insurance Liability Program will temporarily fund the claim settlement/judgment amount until the agency reimburses the program. The agency would then be required to reimburse the Liability Program within their base budget or would have to seek supplemental budget funding

How is biennial funding for the Self Insurance Liability Program determined?
An independent actuarial study is performed each year to provide estimates of the State's total outstanding liabilities at the end of the fiscal year and project liabilities over the next several years. Total outstanding liabilities include the cost over time of resolving all claims from all incidents through the date of the projection. The study also estimates the amount needed to pay claims and tort defense costs over the next several years, estimates total funding needs, and allocates premium to State agencies. Funding proposals and premium allocation formulas are developed by the State's Office of Risk Management (ORM), reviewed by the Risk Management Advisory Committee (RMAC), and approved by the Office of Financial Management (OFM) for inclusion in the Governor's budget.

The Liability Account was originally conceived to provide 100 percent funding for State tort liabilities by accumulating funds over a ten-year period to reach a balance equal to the State's total outstanding liabilities. However, as finally enacted RCW 4.92.130 restricted the Liability Account balance to 50 percent of the estimated total outstanding liabilities. The Liability Account balance reached the 50 percent limit during Fiscal Year 1996, and agency premiums were adjusted accordingly. In subsequent years, funding levels have not reached the 50 percent limit because of the escalating growth of these outstanding liabilities.

What is the most recent actuarial estimate of the state's outstanding liability?
The most recent actuarial study estimated total tort liabilities (claims/indemnity and defense) as of June 30, 2002 at $402.4 million ($259.4 million for claims and $143.0 million for defense costs), increasing to $640.2 million by June 30, 2005 (see chart below).

Estimated Total Outstanding Liability (Millions, Rounded) <u>With</u> Excess Coverage

Fiscal Year	Claim Liabilities	Defense Liabilities	Total
2002	$259.4	$143.0	$402.4
2003	$310.5	$163.6	$474.1
2004	$366.7	$186.3	$553.0
2005	$428.9	$211.3	$640.2

How does the state's total outstanding liability relate to self insurance premium funding?
The funding goal of the SILP is that there will be sufficient cash available to pay projected claim and defense costs and leave the Liability Account with a fund balance at the beginning of each upcoming biennium equal to a target percentage of the state's total outstanding liability for claims. Therefore, the Self Insurance Liability Program's funding level must include the projected amount for actual biennial claims payouts and defense costs, plus an amount to establish a reserve fund balance to start the next biennium.

The following Table illustrates the funding model that was used to develop the overall self insurance premium level for FY03-05:

FY03-05 Premium Increase Required with a 15%, 30% and 50% Reserve Fund Balance ***{Numbers expressed in millions}***			
	15% Reserve	**30% Reserve**	**50% Reserve**
01-03 Ending fund balance (Note 1)	29.53	29.53	29.53
FY04 projected claims costs	45.05	45.05	45.05
FY04 projected defense costs	20.0	20.0	20.0
FY04 excess insurance cost	2.0	2.0	2.0
Total projected FY04 costs	67.05	67.05	67.05
FY05 projected claims costs	48.84	48.84	48.84
FY05 projected defense costs	20.0	20.0	20.0
FY05 excess insurance cost	2.0	2.0	2.0
Total projected FY05 costs	70.84	70.84	70.84
Reserve Amount @ Percentage of Outstanding Liability	64.335	128.67	214.45
Total Premium Required	**173.00 (rounded)**	**237.03**	**322.81**
01-03 Agency Premium	113.11	113.11	113.11
03-05 Additional Premium Required	**59.89**	**123.92**	**209.7**

Note 1: FY01-03 ending fund balance assumes that a $25 million dollar supplemental General Fund-State is funded through the 2003 Supplemental Budget.
Note 2: OFM has decided to fund the Self Insurance Liability Program with a 15% reserve.

How are agency's self insurance premiums allocated?
After the projected funding level is determined, the actuary applies an allocation formula developed by ORM and the Risk Management Advisory Committee to determine each agency's premium. The formula is driven primarily by 5 years of capped losses for each agency and their five-year average FTE count. It is designed to assign premium according to risk. The first step is to establish a statewide rate per FTE, which is done simply by dividing the total number of FTE's into the total amount of premium. Next, agencies are divided into functional groups and a group rate is developed. Then each agency's individual loss experience is considered. For premium purposes only, the actuary uses paid claims and reserves on pending claims during the most recent five years which also have an incident dates within that same five year period. Claims resulting from an accident more than five years ago are excluded. Next a "cap" of $1 million is applied to each claim, meaning any claim paid over $1 million is shown at $1 million regardless of the actual amount paid. Each agency's percentage of capped losses is then compared to their percentage of FTE's and a credibility factor is applied creating an "experience modifier." For example, if an agency has 10% of the group's FTE's but 15% of the capped losses, it is assigned a modifier of l.5. The modifier is then multiplied by the group rate creating an agency rate, which is multiplied by the agencies FTE to arrive at the premium.

What criteria were used to establish a Policy versus Maintenance level decision package?
The placement of the self insurance premium at either the maintenance or performance level of an agency's budget is designed to enhance oversight of agency loss trends and to improve strategies to mitigate future losses. Agencies, whose past and future loss experience are the primary driver of agency premium increase, have been selected to prepare a policy level decision package. Agencies with less frequent and severe losses will complete a maintenance level decision package.

OFM budget and risk management staff jointly developed and employed the criteria used to determine what level of decision packages that agencies prepare. The complexity of the self insurance premium allocation formula necessitated that five criteria be used to determine the level of decision package that an agency should submit. The five criteria are as follows:

- Premium increase of greater than $100,000.
- Total premium greater than $300,000
- Premium increase of greater than 100%.
- Loss experience (modification) factor greater than 1.
- Claims Payout/Premium ratio greater than 75%.

Agencies where at least two of the criteria apply were selected to complete a policy level decision package.

The five criteria helped to identify agencies with greater loss experience, larger total claims payouts, faster growing premiums, and larger premiums. The loss experience (modification) factor measures the relationship between an agency's percentage of the state's total losses divided by an agency's percentage of the state's total FTE's. Higher loss experience ratios highlight those agencies whose FTE's produce a disproportionate share of the risk/exposure. The claims payout/premium ratio greater than 75% identifies those agencies on whose behalf the Self Insurance Liability Program has paid out the most dollars as a percentage of the agency premium contributed.

Total premium increase and total premium size criterion apply to those large agencies that engage in a myriad of function, employ a large number of staff, and use a large fleet of vehicles and other hazardous equipment in their every day operations. The requirement that at least two criteria must apply reduced the number of large agencies, (with total premiums over $300,000) which were required to prepare a policy level package. Seven agencies with total premiums exceeding $300,000 were excluded from preparing a policy level package, because their premiums either decreased or did not increase by over $100,000. Note: The only exception to these criteria applies to small agencies whose total premium is less than $20,000.

What can I do to reduce my agency's risk exposure?

1. If not already done, structure a risk management "function" in the agency. Define roles and responsibilities and inform the management team.

2. Identify the agency's primary risk exposure(s) by:

- Using ORM's Risk Self-Assessment Guide for information on conducting the risk assessment
- Using ORM's Loss History Profile report to pinpoint past loss trends and pending tort loss claims
- Involving agency Attorney General staff and other key managers

3. Set agency risk management goals based on information gathered in risk self-assessment.

4. Establish and carry out action plan for mitigating loss identified in goals.

5. Report on goal progress in budget documents and other management reports.

What services are provided by the Risk Management Administration revolving fund charge?

The Office of Risk Management operational costs will continue to be allocated through the revolving fund adjustment. The charge, called Risk Management Administration, is allocated based on a service driven formula covering claim, commercial insurance and loss prevention services. Eighty percent of the charge is based on the most recent 5 years of claims filed and paid against the agency, weighted 60% for the amount paid on claims and 40% on the number of claims filed. Unlike the self insurance premium, the formula considers all claims during the 5-year timeframe regardless of incident date or amount. Claim services include receipt, processing, investigation, payment and reporting on claims and administration of the Self Insurance Liability Program. Ten percent of the charge is based on each agency's pro rata share of commercial insurance premium paid over the last year. Commercial insurance services include the purchase and administration of a variety of insurance policies and contract insurance and indemnification assistance. The final 10% is based on a modified FTE count . Loss prevention services include loss analysis, agency training and loss prevention consulting.

In addition, the Office of Risk Management invoices agencies for the Department of Transportation's administrative cost to investigate statewide vehicle claims. This charge is allocated to agencies using the most recent 5 years of vehicle claim experience weighted 60 percent for amount paid and 40% for the number of claims file.

Who are the points of contact within the Office of Risk Management if I have questions on any risk management issues?

Loss prevention assessments and goals and agency claim history: Jolene Bellows, 902-7312

Self insurance premium and other risk management issues: Betty Reed, 902-7304